

**STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION**

Commonwealth Edison Company)	
)	Docket No. 05-0597
Proposed general increase in electric)	
Rates, general restructuring of rates,)	
Price unbundling of bundled service)	
Rates and revision of)	
Other terms and conditions of service.)	

REPLY BRIEF OF THE PEOPLE OF THE STATE OF ILLINOIS

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I. INTRODUCTION

NOW COME the People of the State of Illinois (“the People”) and, pursuant to 83 Ill. Adm. Code 200.800, submit this Reply Brief.

II. SUMMARY OF ARGUMENTS

In this Reply Brief, the People respond to arguments presented in Commonwealth Edison’s (“ComEd”) Initial Brief concerning its proposed rate base, operating expenses, revenues and rate design.

A. Rate Base

The People reject ComEd’s arguments regarding its accumulated reserve for depreciation and treatment of its pension contribution. The Commission should reject ComEd’s proposed treatment of its accumulated reserve for depreciation because ComEd’s proposal creates an unbalanced rate base, is contrary to the record established in this case and violates well-founded Commission precedent.

Where consistent with well-founded precedent, the Commission should disallow the Company’s costs of funding its pension contribution. If the Commission decides to allow ComEd to earn a return on the pension contribution, the return should be limited to the actual cost of financing the contribution.

B. Operating Expenses

The People reject several of ComEd’s arguments regarding operating expense, including pension expense, wages and salaries expense, severance costs, incentive compensation, and proposed merger savings. If the Commission decides to allow ComEd to earn a return on the pension contribution and a full year of carrying costs on the pension contribution is included in the Company’s revenue requirement, then the full

annual effect of the contribution on the Company's pension expense should also be recognized.

The Commission should reject ComEd's proposed treatment of its wage and salaries expense, because the record lacks any evidence that its so-called temporary vacancies are actually going to be filled and ComEd does not incur actual expense for vacant positions.

To calculate ComEd's recurring severance costs, the Commission should adopt Mr. Effron's five year average using the years 2001 – 2005 because the year 2000 is not representative of, or relevant to, the expenses that ComEd can be expected to incur prospectively. The Commission should not allow recovery for event-related severance costs because 1) ComEd arguments in favor of recovery are based upon a misunderstanding of Mr. Effron's testimony; 2) ComEd imputes meaning to the Illinois Administrative Code that the Code clearly does not contemplate; 3) the particular facts in this case make recovery unwarranted; and 4) adopting Mr. Effron's position on event-related severance costs denies ComEd double recovery of Exelon Way costs.

The Commission should deny recovery for incentive compensation because ComEd failed to meet the clear standard established by the Commission to justify recovery of such costs.

If the pending merger between Exelon and PSE&G is approved and forecasted merger savings are realized, then those savings should be recognized in this case, so that customers are not left paying rates to recover costs not being incurred by the Company.

C. Revenues

The Commission should adopt Mr. Effron's treatment of revenues, in which he weather-normalized actual test-year revenues to match the Company's use of weather-normalized billing determinants in designing rates resulting in the required revenues.

D. Rate Design

The People reject ComEd's arguments for a single residential rate class. The Commission should adopt the rate design proposed by Mr. Rubin because (1) the Company's own ECOSS favors retaining different distribution rates for heating and non-heating customers; (2) retaining the existing distinction in the customer charge between single- and multi-family customers avoids intra-class cross-subsidization; (3) the Company offers no response to Mr. Rubin's argument that significant differences in meter reading costs between single- and multi-family dwellings warrant different meter rates; and (4) Staff's bill impact mitigation proposal should be applied to recognize differences between residential customers in single- and multi-family dwellings.

The Commission should also reject BOMA and IIEC's minimum distribution study ("MDS") proposal because it does not reflect reality and has been consistently rejected by the Commission.

III. RATE BASE

A. Accumulated Reserve for Depreciation

ComEd's proposal to adjust its rate base for post-test year additions without recognizing the corresponding growth in its reserve for accumulated depreciation should

be rejected because it creates a mismatched rate base, is contrary to the record of the case, and deviates from well-established Commission precedent.

1. ComEd's proposal violates fundamental test year principles by creating a mismatched rate base allowing ComEd to earn a return on an investment not reflected in the test year or 2005.

ComEd has proposed to adjust its rate base for post-test year plant additions without recognizing the simultaneous growth in the reserve for depreciation. *See* AG Ex. 1.0, at p. 8:5-9. The Commission should reject the Company's attempt to earn a return on a net investment in rate base that it did not have at the end of the 2004 test year or the end of 2005.

ComEd states:

Mr. Effron's proposed deduction would deprive ComEd of the full cost recovery to which it is entitled, and would violate fundamental test year principles, which are designed to avoid the very type of mismatched rate base values the AG asks the Commission to approve.

ComEd Initial Brief, at p. 39. On the contrary, Mr. Effron clearly demonstrated, in his direct testimony, that it is ComEd who proposes to violate fundamental test year principles by creating a mismatched rate base.

As Mr. Effron explained, as the future additions take place and increase the balance of gross plant, the accumulated reserve for depreciation will also continue to grow as a result of recording depreciation expense on total plant in service. AG Ex. 1.0, p. 6:3-5. Thus, the net plant in service included in rate base will not increase by an amount equal to future additions. *Id.*, at ll. 5-7. When growth in the balance of the accumulated reserve for depreciation is taken into account, the effect of growth in rate base due to plant additions is mitigated significantly. *Id.*, at ll. 7-9.

Mr. Effron points out the unbalanced nature of the Company's proposal:

This highlights the selective nature of the Company's proposed adjustment to recognize the effect on rate base of post-test year additions to plant in service. It makes little sense to allow a selective pro forma adjustment to increase rate base for post-test year plant additions when the Company's actual growth in the net plant in service, and its rate base, will be substantially less.

AG Ex. 1.0, at p. 6:9-14. The Commission should reject ComEd's attempt to earn a return on a net investment in rate base that it did not have at the end of the test year or the end of 2005.

2. ComEd's proposed treatment of its reserve for accumulated depreciation is contrary to the record established in this case.

ComEd claims:

His [Mr. Effron's] proposed adjustment reflects a change to one component of rate base for no supportable reason other than the attrition that has occurred to the book value of ComEd's plant in service at year end 2004 with the passage of one additional year.

ComEd Initial Brief, at p. 39. ComEd's statement is both false and contrary to the record established in this case.

On cross-examination, Mr. Effron clearly stated,

Other than the passage of time, what is happening as the Company is making these plant additions, they are also recovering real dollars from customers for the return of the plant in service as of December 31, 2004. The customers are paying rates that include as an element a capital consumption allowance, depreciation.

As the customers pay for the Company's service, the cost of that service which determines the rates that they pay include recovery of plant in service. As the Company is making additions to plant in service, in 2005, the Company is also recovering the cost of the embedded plant in service in 2004.

Tr. at p. 1614:16-22 – p. 1615:1-7. Thus, the growth in accumulated reserve for depreciation is not simply representative of the attrition that has occurred to the book value of ComEd's plant in service at year end 2004 with the passage of one additional year. In fact, it represents the actual recovery of the cost of plant from customers as the Company recovers a revenue requirement that includes depreciation expense as an element of the cost of service. See *id.*

It would be inequitable, inconsistent and inappropriate to recognize growth in rate base related to post-test year plant additions without recognizing the simultaneous recovery of the cost of plant in service from customers, and therefore, the Commission should reject the Company's proposal.

3. The Company's proposal violates well-founded Commission precedent.

Attempting to distinguish established precedent on the treatment of reserve for accumulated depreciation, the Company misrepresents the decisions cited by Mr. Effron to support his proposal. The Commission should adopt the same treatment in this case as it did in ICC Docket No. 03-0009 (Cons.) and offset the post test year additions to plant with the post test year growth in depreciation reserve, to avoid a mismatch of the elements of rate base.

ComEd argues that none of the cases cited by Mr. Effron in his revised rebuttal testimony, *In re Illinois Power Co.*, ICC Docket. 01-0432 (Order, March 28, 2002), *In re Central Illinois Light Co.*, ICC Docket 02-0837 (Order Oct. 17, 2003), and *In re Central Illinois Public Service Co. (AmerenCIPS) and Union Electric Co. (AmerenUE)*, ICC Docket 02-0798, 03-0008, 03-0009 [Cons.] (Order, Oct. 22, 2003), support Mr. Effron's

proposed adjustment. ComEd Initial Brief, at p. 41 (*citing* Effron Reb., AG Ex. 3.0 Corr., 11:3-12). Attempting to distinguish these cases, the Company argues,

Unlike in this case, the decisions cited by Mr. Effron involve situations in which the Commission found that historical plant in service was either declining or static, requiring further analysis of post test year *pro forma* increases in plant in service to avoid an increase to rate base when, in fact, after netting out the effect of declining plant in service and Depreciation Reserve with the *pro forma* additions, there should have been a decrease in rate base.

ComEd Initial Brief, at p. 41.

In fact, with regards to both *In re Illinois Power Co.*, ICC Docket. 01-0432 (Order, March 28, 2002) and *Union Electric Co. (AmerenUE)*, ICC Docket 02-0798, 03-0008, 03-0009 [Cons.] (Order, Oct. 22, 2003), there was no finding that “historical plant in service was either declining or static.” In both of these cases, plant in service was growing, but, as with ComEd, such growth was found to be offset by growth in the reserve for depreciation. Further, in both of those cases, the Commission properly offset the adjustment for plant additions with the concomitant growth in the reserve for depreciation.

In *(AmerenCIPS) and Union Electric Co. (AmerenUE)*, ICC Docket 02-0798, 03-0008, 03-0009 [Cons.] (Order, Oct. 22, 2003), the Commission clearly acknowledged that the *AmerenUE* net plant balance was increasing, but found “that UE's proposed additions to plant in service should be included in rate base” only “to the extent that they exceed increased accumulated depreciation.” *See* Order, Docket No. 03-0009, at pp. 10-11. The Commission concluded that this treatment “more accurately matches the costs and revenues that may be expected for the period during which the rates are in place.” *See id.*

There is no basis to distinguish the situation of ComEd from that of *AmerenUE* in Docket No. 03-0009. The Commission should adopt the same treatment in this case that it did in Docket No. 03-0009 (Cons.) and offset the post test year additions to plant with the post test year growth in depreciation reserve, to avoid a mismatch of the elements of rate base.

B. Pension Contribution

If the Commission decides to allow ComEd to earn a return on the pension contribution, the return should be limited to the actual cost of financing the contribution. AG Initial Brief, at p. 6.

ComEd states, “[t]he contribution ComEd made to its pension fund was not funded by a debt issuance at ComEd.” ComEd Initial Brief, at p. 63. It is undisputed that Exelon funded the contribution by issuing debt. *See* AG Initial Brief, at pp. 6-7. The subsequent accounting machinations that make this debt ultimately appear on the books of ComEd as equity do not change this underlying reality.

Accordingly, any return on ComEd’s pension contribution should be limited to the cost of debt issued specifically for the purpose of making the pension contribution. *See* AG Initial Brief, at pp. 9-10. This can be accomplished by: 1) removing the contribution from rate base, 2) removing the “equity” related to the pension contribution from the Company’s capital structure, and 3) including the interest on the pension contribution in pro forma test year operating expenses. *Id.* Alternatively, the same end could be achieved by reclassifying the \$803 million related to the pension contribution from equity to debt in the Company’s capital structure. *Id.* ComEd has not provided any legitimate reason to treat this debt financing as an equity contribution. Therefore, where

the Commission allows any return on this pension contribution, the Commission should apply Mr. Effron's adjustment in one of the manners provided.

IV. OPERATING EXPENSES

A. Pension Expense

ComEd suggests that a full year's effect of the pension contribution should not be reflected in the Company's pension expense because the effect of the contribution will not be realized until 2006. *See* ComEd Initial Brief, at p. 69. However, if the Commission does not accept Staff's proposed treatment of the pension contribution, and a full year of carrying cost on the pension contribution is included in the revenue requirement, the full annual effect of the contribution on the Company's pension expense should also be recognized. *See* AG Initial Brief, at p. 12. The annual effect of the pension contribution is to reduce the jurisdictional expense by \$8,563,000 from the expense included by ComEd in its revenue requirement. *See id.*

B. Wages and Salaries Expense

The Company's arguments on the proper number of employees to use for the purpose of calculating the appropriate pro forma wage and salary expense ask the Commission to believe what the evidence not only fails to show, but also contradicts. The Company argues strenuously that the vacancies that existed at the end of 2004, the vacancies that continued into 2005, and the vacancies that had *increased* by the end of 2005, are some how "temporary" in nature. ComEd Bf. at 113-114. The Company's assertions that these vacancies are about to be filled momentarily would have more persuasive value if there were *any* evidence that the so-called temporary vacancies were actually being filled. The Company has produced no such evidence.

For example, to support its contention that the vacant positions are being filled, ComEd noted that “as of the end of 2005, the number of ComEd employees had increased again to within 1% of year-end 2004 levels”. ComEd Ex 13.0 at 35. In fact, this is evidence that ComEd has *not* been filling the vacant positions. As of December 2005, there were 5,473 full time equivalent employees. Tr. at 235-6; AG Cross Ex. 2. That number is not only less than the 2004 year-end number of employees and 2004 average number of employees, it is also slightly less than the average number of employees for the six months ended September 2005 (5,482), the period that Mr. Effron used to quantify his proposed adjustment. AG Ex. 3.0 at 13. If anything, the actual number of employees as of December 2005 confirms the reasonableness of Mr. Effron’s adjustment. It certainly does not show that the employee complement is increasing as the result of vacant positions being filled. The actual number of employees as of December 2005 is just further evidence that the average number of employees in 2004 (even after adjustment for the ExelonWay program) is not representative of the Company’s prospective employee complement. AG Ex. 1.0 (Effron rebuttal) at 2-3.

ComEd argues “that the positions have not yet been filled is besides the point.” ComEd Bf. at 114. On the contrary, that is exactly the point. Who is the Commission to believe, ComEd whose claims are unsupported by any tangible evidence, or actual experience, which shows a continuing decline in the number of employees?

ComEd claims that:

Mr. Effron arrived at his specific adjustment based on results-oriented mathematical manipulations which are patently unfair. At the time his written testimony was prepared, Mr. Effron had available 9 months of 2005 employee data running through September 2005. Effron Dir., AG Ex. 1.0, at 18:20-21. Instead of using that data, Mr. Effron employed a “six month average” for his employee count and based that average upon

“the six months ended September 2005.” Effron Dir., AG Ex. 1.0, at 18:20. Not surprisingly, the average employee count for the full nine months of 2005 – 5,503 – was higher than the average for the six month period Mr. Effron used – 5,482. Tr. at 1627:9-1628:5

ComEd Bf. at 114.

It is not surprising at all. The simple reason that the average employee count for the full nine months of 2005 was higher than the average for the six month period used by Mr. Effron is that the number of ComEd distribution employees continued to decrease through 2005. As a simple matter of mathematics, adding earlier months in the calculation of the average is going to increase the average when the number of employees is declining. If it were Mr. Effron’s intent to use the lowest number of employees, he could have updated his adjustment to use the average number of employees for the six months ended December 31, 2005, or, alternatively the nine months ended December 31, 2005. Either of these methods would have yielded a lower number of average employees than the six month period used by Mr. Effron. This analysis indicates that, if any party is performing “results-oriented mathematical manipulations which are patently unfair” it is the Company. “Not surprisingly” ComEd must resort to such manipulations, as there is no actual evidence to support its claim that the “temporary” vacancies are going to be filled at any time in the foreseeable future.

ComEd does not incur actual expense related to vacant positions. The Commission should not include salaries for non-existent employees in the Company’s revenue requirement. The Company has no problem adjusting test year wages and salaries for post test year changes that increase expenses – such as wage rate increases. ComEd Ex. 19.0 at 44. The same recognition should be given to factors decreasing wage and salary expenses – such as a decrease in the number of employees, especially when

there is no tangible evidence that the decrease will be reversing at any time in the near future. For these reasons, the Commission should disregard ComEd's arguments and accept Mr. Effron's adjustment to wages and salaries as just and reasonable.

C. Severance Costs

1. Recurring Severance Costs

The only issue raised by ComEd was whether the five year average should be based on the years 2000 – 2004, or the five years 2001 – 2005. While the Company argues that Mr. Effron's exclusion of the year 2000 from his proposed average is unjustified (*see* ComEd Initial Brief, at p. 116), there can be no dispute that the five year period 2001-2005 is more recent. *See* People's Initial Brief, at p. 16.

In fact, the only reason to reach back to 2000 is to artificially inflate the level of recurring severance costs by reflecting a year that is an obvious outlier. A review of the Company's experience in the years 2000 through 2005 shows that no other year was even close to the \$5.8 million incurred in 2000. ComEd Ex. 19.0, Schedule 16, Page 1. The next highest year was the \$1.4 million incurred in 2003. *Id.* The recurring severance expense booked by the Company in 2000 is not representative of the expense incurred in the years since, and there is no reason to believe that it is in any way relevant to the expenses that ComEd can be expected to incur prospectively. As such, there is no reason to include 2000 in the average level of recurring severance expenses other than to distort the average used to determine the normalized level of expense.

2. Event-Related Severance Costs

- a. ComEd's arguments are based upon a misunderstanding of Mr. Effron's testimony.

At the outset, ComEd's arguments reveal an ongoing misunderstanding of Mr. Effron's proposal regarding event-related severance costs. ComEd repeatedly states that Mr. Effron recommends disallowing the severance costs from the Exelon Way initiative entirely because "the savings allegedly will not be recovered in rates." ComEd Initial Brief, at p. 118. Mr. Effron never alleged that the savings will not be recovered in rates. In fact, Mr. Effron's rebuttal testimony states just the opposite, that the savings will be reflected in rates when the rates in this case go into effect. *See* AG Ex. 3.0R, at p. 16:8-9.

Later in its Initial Brief, ComEd states:

Mr. Effron also claims that recovery is improper because the future savings will not be reflected in rates, and therefore "the savings retained by shareholders will have more than paid for the costs of the program by the time the Commission issues an Order in this case."

ComEd Initial Brief, at p. 120. This argument again misrepresents Mr. Effron's testimony. Mr. Effron never claimed that "the future savings will not be reflected in rates." In fact, as noted above, he stated just the opposite in his rebuttal testimony - that the savings will be reflected in rates when the rates in this case go into effect. AG Ex. 3.0, 16: 8-9, *supra*. What Mr. Effron did state, and what is not in dispute, is that, prior to the rates going into effect, the savings from the Exelon Way program have been and are being retained by shareholders. *See id*, ll. 9-12. It is undisputed that the cumulative savings by the end of 2006 will have exceeded the cost of the program. The Company's arguments are thus obviously based on a misunderstanding of Mr. Effron's testimony.

- b. ComEd imputes meaning to Ill. Admin. Code 285.3215 that clearly is not contemplated by the rule.

The Company's attempt to magically impute a "mechanism for utilities to recover costs related to a costs savings program" into Illinois Administrative Code Part 285.3215

fails miserably. *See* ComEd Initial Brief, at p. 119. A simple reading of the cited section reveals that Part 285.3215 does nothing more than set out the information that the Company must provide when it is seeking to recover costs associated with cost savings programs. 85 Ill Admin. Code. 285.3215. There is absolutely nothing in this section that “provides a mechanism for utilities to recover costs” related to cost savings programs. Further, there is absolutely nothing in this section that describes the circumstances under which such costs should be recoverable, much less implies that recovery of such costs must be allowed. Rather, whether such should be allowed depends on the particular circumstances of the case.

The Company uses Part 285.3215 to argue that costs related to a cost savings program should automatically be recovered. This position conflicts with basic tenants of rate making contained in the Public Utilities Act. ComEd states, “the entire point of Section 285.3215 is to allow recovery of the “initial costs” of “cost savings initiatives...”” *See* ComEd Initial Brief, at p. 119. ComEd then criticizes Mr. Effron for not referencing Part 285.3215 in his direct or rebuttal testimonies.

The Act states that “the Commission shall establish the rates or other charges...which it shall find to be just and reasonable.” 220 ILCS 5/9-201(c). The only bearing that Section 285.3215 has on this issue is that it sets out the information that the Company must provide when it is seeking to recover costs of programs to reduce expenses. There is absolutely nothing in Section 285.3215 to suggest that its “entire point” is “to allow recovery of the ‘initial costs’ of ‘cost savings initiatives’ without regard to whether those costs recur” or, for that matter, to allow recovery of such costs at

all. The decision of whether to allow recovery of costs rests with the Commission upon a determination of those costs as just and reasonable.

Further, there would be no logical reason for Mr. Effron to reference Section 285.3215 in his direct or rebuttal testimony, as that section imposes information requirements on the utility, not on other parties. It is true that there would be little point to Section 285.3215 if utility companies were not to be afforded an opportunity to recover severance costs when the purpose of the severance program is to recover expenses. However, whether such costs should be included in the prospective revenue requirement must depend on the particular facts, and Section 285.3215 does nothing to alter this basic principle.

- c. Recovery of event-related severance costs is not appropriate in this case.

To determine whether recovery of severance costs related to the Exelon Way program is just and reasonable, it is useful to summarize the facts not in dispute with regard to the severance expenses related to the Exelon Way program: 1) The costs of the Exelon Way program were incurred in 2003 and 2004, four and three years, respectively, prior to the time that the rates established in this case will go into effect; 2) By the time that the rates go into effect, the program will have generated over \$210 million in savings in the years 2004 – 2006; 3) These savings were not reflected in the rates paid by customers; 4) The cumulative savings in the years 2004 – 2006 substantially exceed the costs of the Exelon Way program. *See* AG Ex. 3.0R, at p. 16:1-16; *see also*, ComEd Ex. 19.0, Schedule 16, p. 2. Given these facts, the only conclusion is that there is nothing left to recover. While there are cases where the costs of a severance program should be recoverable in rates prospectively, this is clearly not one of those cases.

- d. Mr. Effron's proposed adjustment to event-related severance costs denies ComEd double recovery of the Exelon Way costs.

ComEd complains that Mr. Effron's proposed adjustment "would deny ComEd any recovery of that cost (initial severance costs associated with the Exelon Way Program), which removes the incentive created by Section 285.2315 to initiate such programs." *See* ComEd Initial Brief, at p. 121. However, Mr. Effron's adjustment does not deny ComEd recovery of the cost of the Exelon Way program. It is undisputed that the savings retained by shareholders are greater than the costs of the program. *See* AG Ex. 3.0, at p. 16:9-12. Thus, ComEd has already recovered the costs. When the savings retained by shareholders are greater than the cost of the program, every incentive necessary to undertake the program exists. The only thing that Mr. Effron's proposed adjustment would deny ComEd is a double recovery of the Exelon Way costs – once from savings already retained by shareholders and a second time in rates paid by customers. *See id.*, at ll. 14-16.

D. Incentive Compensation

ComEd argues in its Initial Brief that the People and the Staff cannot require it to show "tangible or quantifiable results and the specific dollar savings or other tangible benefits conferred upon ratepayers from [ComEd's] incentive compensation plan," stating:

Mr. Effron claims that ComEd must prove that incentive compensation will "reduce expenses and create greater efficiencies in operations." Effron Dir., AG Ex. 1.0, at 20:8-10. Ms. Ebrey and Mr. Effron demand more than the Commission requires, or properly could require.

ComEd Bf. at 136-137. ComEd further argues that:

Ms. Ebrey and Mr. Effron insist upon evidence that ComEd, or any other utility, simply cannot provide. As such, their approach to incentive compensation serves only to thinly disguise a pre-determined decision to deny recovery: *i.e.*, they purport to base their opposition to recovery on a test, but that test can never be met.

ComEd Bf. at 137.

Contrary to the Company's characterization, the cited quote is not a "claim" by Mr. Effron or by Staff. It is the standard for recovery of incentive compensation clearly established by the Commission as set out in the People's Initial Brief. People's Int. Bf. at 17, *citing* (Docket No. 01-0432, *Illinois Power Company*, Order, March 28, 2002, at 42-43 and Docket No. 04-0779, *Nicor Gas Company*, Order, September 20, 2005, at 44-46).

The Company does not contend that Mr. Effron has misrepresented the Commission's standard for recovery of incentive compensation. Thus, the Company's quarrel is not really with Mr. Effron or Staff, but rather with the Commission. The Company explicitly admits that it cannot provide the evidence required by the Commission. ComEd Bf. at 137. Accordingly, its request to recover its incentive compensation expense from ratepayers should be denied.

1. ComEd cannot disregard the Commission incentive compensation test.

Instead of addressing the Commission test for recovery of incentive compensation plan costs, ComEd argues that it "must offer incentive competition in order to provide the competitive compensation package necessary to attract and to retain high-quality employees." ComEd Bf. at 122. The People do not argue that all incentive compensation costs are per se unrecoverable. Rather, the People's position is that incentive compensation costs must meet the Commission-applied test in order to be recoverable in just and reasonable rates.

The Commission made its position on incentive compensation clear:

IP should not be allowed to recover from ratepayers the expenses associated with its current incentive compensation plan. First,...the Commission has generally disallowed such expenses except where the utility has demonstrated that its incentive compensation plan has reduced expenses and created greater efficiencies in operations. For example in the CILCO proceedings in Dockets 99-0199/99-0131 (Cons.), the Commission disallowed such expenses, and in doing so stated on pages 37-38, “The Commission remains convinced that such expenses are not recoverable in the absence of any evidence that the...Plan benefits ratepayers.” In the limited number of cases, in which such expenses were allowed, those companies had historical patterns of paying incentive compensation and were able to demonstrate that the incentive compensation payments provided benefits to ratepayers.

ICC Docket No. 01-0432, *Illinois Power Company Proposed Revisions to Delivery Tariff Sheets*, Order, March 28, 2002 at 42-43. The Commission reiterated that position in *Consumer Illinois Water*, stating “to recover incentive compensation, the plan must confer upon ratepayers specific dollar savings or other tangible benefits.” 03-0403 *Consumers Illinois Water*, Order, April 13, 2004, at 15.

ComEd has failed to introduce evidence to meet the Commission standard, and therefore, its incentive compensation plan costs are not recoverable. As stated in the People’s Initial Brief, ComEd’s argument that incentive compensation is a common component of utility salaries does not give ComEd a free pass on the incentive compensation test. People’s Int. Bf. at 17, *citing Nicor Order* at 45. ComEd’s entreaties for the Commission to completely discard the test, because it “has outlived its usefulness”, does not itself hold water. ComEd Bf. at 140. ComEd’s claim that incentive compensation is widely used ignores that it is the goals and effect of the plan that are evaluated, not the mere existence of the plan. Therefore, ComEd’s arguments miss the

point. The Commission should continue to apply its incentive compensation test, as set out in the cases above, and deny recovery of ComEd's incentive compensation plan costs.

2. ComEd has not met the Commission incentive compensation test.

ComEd offers that its “dramatically improved” reliability and lower outage frequency constitute tangible customer benefits. ComEd Bf. at 136. ComEd, however, has not shown that these benefits were specifically attributable to the incentive compensation plan and not other initiatives to meet ComEd's existing service obligations. ComEd's argument allows any customer benefit currently enjoyed to be linked to the incentive compensation plan. ComEd has not demonstrated how the financial goals, upon which the incentive payments are based, translate into specific dollar savings to customers or tangible customer benefits.

ComEd further argues that the financial goals of its incentive compensation plan “inure to the benefit of customers.” ComEd Bf. at 137. These theoretical trickle-down benefits are not sufficient to meet the Commission incentive compensation test. Where an incentive compensation plan is triggered by attaining financial goals and thereby primarily benefits shareholders, it is proper that shareholders, not ratepayers, bear the cost of obtaining those benefits. Therefore, the People request the Commission follow its current practice and disallow recovery of ComEd's incentive compensation plan costs.

E. Merger Savings

As stated in the People's Initial Brief, Exelon and PSE&G offered, before the New Jersey Board of Public Utilities (“BPU”), that projected savings that would result from the merger as a justification for the merger. People's Bf. at 18. If the savings are certain enough to be used for this purpose, then they are certain enough to take into

consideration in the determination of the Company's revenue requirement in this case. If the merger is approved and the forecasted savings are achieved, absent any recognition of those savings in this case, customers will be paying rates to cover costs not being incurred by the Company.

V. REVENUES

ComEd completely disregards the People's adjustment to its proposed revenues. In order to calculate pro forma test year operating income under present rates, the Company should have weather-normalized its actual test year revenues. The Company uses weather normalized billing determinants to design rates that will result in the required revenues. *See* AG Ex. 1.0, at p. 15:15-17. However, the actual test year revenues were not weather normalized for the purpose of calculating pro forma test year operating income under present rates. *Id.*, at ll. 17-18. This unbalanced application of weather normalized data does not provide an accurate picture of test year revenues. *See* People's Initial Brief, at p. 20.

Mr. Effron adjusted the Company's proposal by increasing test year revenues by \$32,796,000 to correct the Company's failure to weather-normalize actual test year revenues. *See* AG Initial Brief, at p. 20. This increase to revenues reduced the Company's revenue deficiency but did not affect the Company's revenue requirement and should not affect the rate design. *Id.*

ComEd has effectively waived any arguments it may have had against Mr. Effron's proposal by stating, "[t]here does not appear to be a material contested issue on this subject." ComEd Initial Brief, at p. 151.

VI. RESIDENTIAL RATE DESIGN

ComEd does not adequately respond to the People's rate design proposal, which retains existing rate distinctions. Retaining separate rates for (1) distribution charges of heating and non-heating customers, (2) customer charges between single- and multi-family customers, and (3) metering charges of single- and multi-family customers comports with the Company's own Cost of Service Study ("COSS"). Also, the Commission's mitigation plan should be applied to recognize the difference in rates between single- and multi-family customers. Finally, the Commission should reject the Minimum Distribution Study proposal set forth by the Building Owners and Managers Association ("BOMA") and the Illinois Industrial Energy Consumers ("IIEC") because it is unrealistic and has been consistently rejected by the Commission.

A. The Company's Own Cost of Service Study Argues in Favor of Retaining Different Distribution Rates for Heating and Non-Heating Residential Customers.

ComEd avoids responding to the People's proposal to retain separate distribution rates for heating and non-heating residential customers by continually confusing the total cost to serve customers with the rate per Kilowatt Hour ("KWH") charged to customers. Contrary to ComEd's argument, if the total cost to serve two customers is the same, it does not follow that the per-KWH rate charged to each customer should also be the same.

To justify eliminating the existing distinction in the distribution rate between heating and non-heating customers, ComEd argues, "[e]nd-use characteristics and customer load shape do not contribute to distribution costs to any significant degree." ComEd Initial Brief, at 189. ComEd goes on to state, "ComEd's costs generally are not affected by the characteristics of the customer's end-use of the electricity." *Id.*, at 194.

Accepting these two statements, it necessarily follows from the Company's own cost of service study that setting the same rate per KWH would result in the over-recovery of costs from high-use customers and the under-recovery of costs from low-use customers.

Using the Company's own ECOSS, Mr. Rubin found that the difference in the level of consumption between heating and non-heating customers means that there should be a difference in the per KWH distribution charge of between 10%-15%. *See People's Initial Brief*, at 31. ComEd refers to this difference as "miniscule," but its own witness contradicts this contention. *ComEd Initial Brief*, at 194. Mr. Crumrine expressed support for different rates between Small Load and Medium Load classes, where there is only a 4.5% difference between the Small Load and Medium Load classes' distribution costs, recovered through the distribution charge. Therefore, the greater difference in distribution costs between space-heating and non-heating customers clearly justifies separate rates for these two classes under the Company's own criteria. *People's Initial Brief*, at 31.

The Commission should reject ComEd's continuous failure to recognize the difference between the cost per customer of providing distribution service and the amount of the charge per KWH that should be charged, and retain the existing distinction between distribution rates for heating and non-heating residential customers.

B. Retaining the Existing Distinction in the Customer Charge of Single- and Multi-Family Customers Avoids Intra-Class Subsidization.

ComEd argues, "[p]roper customer class delineations avoid, to the extent possible, the creation of intra-class subsidies." *ComEd Initial Brief*, at 189. However, eliminating the existing distinction in the customer charge between single- and multi-

family customers would result in multi-family customers subsidizing single-family customers, violating the Company's stated purpose.

ComEd cites to a workpaper from its ECOSS entitled, "Unit Delivery Cost for Current Residential Sub-Classes." *See id*, at 191. While the table itself is accurate, the conclusions ComEd draws from the table are incorrect. The table clearly shows that customer-related costs for single-family customers approaches \$8 per customer per month (Single-Family Without Space Heating = \$7.74; Single-Family With Space Heating = \$8.02). In contrast, it shows that customer-related costs for multi-family customers fall under \$6 per customer per month (Multi-Family Without Space Heating = \$5.91; Multi-Family With Space Heating = \$5.86). *Id*. Customer related costs are fully one-third higher for single-family customers than they are for multi-family customers, under the Company's analysis.

The critical difference between the Company's treatment of the customer charge and Mr. Rubin's proposal is that the Company seeks to simply average these four different charges together, resulting in multi-family customers subsidizing single-family customers. This result directly contradicts ComEd's stated purpose of avoiding intra-class subsidies. *See* ComEd Initial Brief, at 189, *supra*. Therefore, the Commission should reject ComEd's proposal and retain separate customer charges for single-family and multi-family customers.

C. The Company Fails to Respond to the People's Argument that Significant Differences in the Cost of Reading Meters in Single- and Multi-Family Dwellings Warrant Separate Metering Rates.

The Company completely misrepresents the People's proposal to retain separate metering rates for single- and multi-family customers. First, the Company discusses

meter installation, an issue that was not the basis for Mr. Rubin's adjustment to the Company's proposal. Second, the Company suggests that the People's proposal ignores urban and suburban distinctions within its service territory, when in fact, this distinction forms the basis of the People's proposal.

1. Mr. Rubin did not consider meter installation cost differences in his adjustment to the Company's metering rates.

ComEd continuously refers to People's assertions "that meter installation...costs are lower for multi-family residences." *See* ComEd Initial Brief, at p. 192; *see also id.*, at p. 193. However, Mr. Rubin's adjustment to ComEd's proposed metering rates is not based on the differences in installation costs.

In his direct testimony, Mr. Rubin mentions that he expects meter-related efficiencies in serving multi-family buildings, such as lower installation costs per unit. *See* AG Ex. 2.0, at p. 19:409-410. However, Mr. Rubin clearly identifies the basis of his adjustment to ComEd's meter charge just a few lines later.

To be conservative, however, I have not made a further adjustment to the metering costs to reflect such a difference.

* * *

Thus, I have only adjusted the meter reading cost, based on differences in meter reading efficiency.

AG Ex. 2.0, at p. 20:416-419. The Company's references to the People's adjustments based upon meter installation costs are unresponsive and should be rejected.

2. The People's metering costs proposal is based upon the real difference in cost between reading meters in urban, suburban and rural areas.

The Company states, "the AG ignores the fact that ComEd's service territory is a mix of urban and suburban areas that contain both single- and multi-family dwellings."

ComEd Initial Brief at 193. This statement is completely incorrect as the People, in the absence of any record evidence provided by the Company, based its proposal on the real difference in costs between reading meters in urban, suburban and rural areas.

The Company failed to provide any actual data on meter-related cost differences between single- and multi-family customers. *See* People's Initial Brief, at pp. 29-30. In the absence of any objective record evidence, Mr. Rubin relied on an independent industry survey by the Ascent Group, which found that reading meters in densely-populated areas is far more efficient than reading them in less densely-populated areas. *See id.* In contrast, the Company, while failing to provide any record evidence to support its position, proposes to collapse the metering rates of single- and multi-family customers, effectively treating every residential customer throughout its service area the same – a position not supported by the record and bearing no relationship to reality.

D. Staff's Mitigation Proposal is Consistent with the People's Rate Design Proposal, and Should be Applied to Recognize Differences Between Residential Customers in Single- and Multi-Family Buildings.

The Company argues that the mitigation proposal adopted by the Commission in ICC Docket No. 05-0159 is inconsistent with the AG's proposal to maintain the single- and multi-family distinctions. *See* ComEd Initial Brief, at p. 193. However, the Commission's mitigation process is based only upon the bill impacts of an average heating customer and an average non-heating customer; not on single- and multi-family distinctions. *See* People's Initial Brief, at p. 23. Specifically, Staff Witness Lazare, the designer of the mitigation proposal in the procurement case, confirmed that it does not address customer impacts in the delivery service tariff case, specifically with regard to low-use multi-family residents. *See* People's Initial Brief, fn. 15, pp. 23-24. Considering

the impact to low-use multifamily customers discussed in the People's Initial Brief (115%-125%), the Commission mitigation plan should be applied to recognize differences between single- and multi-family customers. *See* People's Initial Brief, p. 26.

E. The Commission Should Reject BOMA's and IIEC's Minimum Distribution Study Proposal Because it Does Not Reflect Reality and Has Been Consistently Rejected by the Commission

The Company should not employ the minimum distribution study ("MDS"), proposed by IIEC witness Chalfont, in determining just and reasonable rates. Employing the IIEC's MDS proposal is not appropriate for several reasons. First, the Commission has consistently rejected MDS over the last 15 years. *Central Illinois Public Service Co. and Union Electric Co.*, Docket No. 00-0802, 214 PUR 4th 437 (2001); *Central Illinois Public Service*, Docket No. 99-0121, 1999 Ill. PUC LEXIS 646 (1999); *Peoples Gas Light and Coke Co.*, Docket No. 91-0586, 1992 Ill. PUC LEXIS 376 (1992); *Illinois Power Co.*, Docket No. 91-0335, 1992 Ill. PUC LEXIS 267 (1992); *Commonwealth Edison Co.*, Docket No. 90-0169, 1991 Ill. PUC LEXIS 99 (1991); *Illinois Power Co.*, Docket No. 90-0006, 117 PUR 4th 418 (1990); *Northern Illinois Gas Co.*, Docket No. 88-0277, 103 PUR 4th 290 (1989). As the Commission has articulated:

[D]istribution systems are designed primarily to serve electric demand, and the Commission agrees with Staff that attempts to separate the costs of connecting customers to the electric distribution system from the costs of serving their demand remain problematic. Furthermore this conclusion is consistent with decisions in recent cases...

Central Illinois Public Service Co. and Union Electric Co., Docket No. 00-0802, 214 PUR 4th 437 (2001).

Second, the concept of a "minimum" distribution system, unrelated to energy consumption, is entirely theoretical and bears no relationship to the actual cost incurred

by utilities to serve actual customers. Indeed, the Commission directly cited this defect in a previous ComEd case, holding:

Edison objected to Mr. Corbin's suggestion that Edison perform a minimum distribution study... Edison also contended that little useful information would be gained from further analysis for the following reasons: 1) the determination of what constitutes a minimum distribution system is almost entirely arbitrary; and 2) **such an analysis is highly theoretical and bears no relationship to any utility's actual engineering practices.** Real systems are built to accommodate expected rather than minimum loads.

The Commission agrees with Edison that performing a minimum distribution system analysis would require substantial time and resources, but would produce no commensurately worthwhile results.

Commonwealth Edison Co., Docket No. 90-0169, 1991 Ill. PUC LEXIS 99 (1991)

(emphasis added). Assuming that a zero-use customer would be connected to the distribution system, as Mr. Chalfant does, is not realistic. A customer will connect to the system to use electricity, and the utility will incur costs based on the customer's anticipated demand for electricity. AG Ex. 2.13 at 3-4.

Finally, Mr. Chalfant fails to quantify the impact of his MDS proposal. The People's witness Rubin, however, estimated that Mr. Chalfant's MDS proposal "would result in enormous shifts in cost allocation among customer classes." AG Ex. 2.13 at 4. Under the low end of Chalfant's proposal, these shifts would nearly double the level of rate increase proposed by ComEd for the residential classes, and more than triple the rate increase for the watt-hour class. AG Ex. 2.13 at 5. If those shifts in cost were made, the non-residential small load, medium load, large load and very large load classes would benefit. Indeed, rates for the small load and medium load customers, proposed to increase by \$15.7 million and \$29.9 million respectively, would actually decrease below current rates under Chalfant's proposal, with those costs shifting to residential customers.

AG Ex. 2.13 at 5. Moreover, adopting Mr. Chalfant's MDS approach would result in an enormous shift in cost allocation that bears absolutely no relationship to the actual cost incurred to design and construct ComEd's distribution system. AG Ex. 2.13 at 6.

The MDS proposal has no merit. ComEd's proposed method of allocating distribution lines and transformer costs on the basis of customer demand is fully consistent with Commission precedent, fully consistent with the way in which distribution systems are designed and constructed, and directly related to the way in which customers use the distribution system. AG Ex. 2.13 at 6. There is no reason to over-turn long-standing Commission practice that consistently and properly rejects the theoretical MDS concept. Therefore, the Commission should reject the MDS proposal.

F. Rate Design Conclusion

Consistent with the record created in this docket, the Commission should reject ComEd's unresponsive arguments and retain existing distinctions between residential single- and multi-family customers and residential heating and non-heating customers. The Commission should also apply the Commission's bill-impact mitigation proposal to recognize differences between multi- and single-family customers. Finally, the Commission should reject BOMA's and IIEC's MDS proposal because it does not reflect reality and has been consistently rejected by the Commission.

V. CONCLUSION

WHEREFORE, for the above stated reasons, the People request that the Commission enter an order establishing just and reasonable rates for Commonwealth Edison based upon the People's arguments presented above and in their Initial Brief.

Respectfully Submitted,
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